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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

No. 87-304

WILLIAM LEIGHTON,

Petitioner, Objector-Appellant

v.

BEATRICE COMPANIES, Inc. et al.

Kohlberg, Kravis, Roberts & Co.

and Joel B. Smilow,

James L. Dutt,

Respondents, Defendants-Appellees.

PETITIONER'S REPLY BRIEF AND APPENDIX

On Petition for Certiorari to

the Supreme Court of Delaware

William Leighton

249 West 11th Street

New York, N.Y. 10014

(212)255-0001

September, 1987

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PETITIONER'S REPLY BRIEF

Since the respondents have moved the Court to deny the petition for certiorari for want of jurisdiction, the allegations of the petition and of this reply brief should be deemed to be true for want of contrary findings by the courts below.

The obfuscation below.

The respondents have deliberately confused the courts below as early as April 11, 1986 by filing a misleading "opinion letter" with the Chancellor, three days before the "fairness" hearing. The letter is reproduced in full in the appendix to this reply, R.88a ff. The purpose of the letter was not only to confuse the Chancellor concerning this case but also to prevent him from ruling on contentions that would have been fatal to KKR's designs on Safeway, Owens Illinois and Jim Walter Corporation, all of which were taken over by KKR after the

Beatrice episode. Beatrice, Safeway, Owens-Illinois and Jim Walter were all listed stocks on the New York Stock Exchange.

KKR's assault upon Beatrice had to succeed in order to make the other assaults possible.

If the assault on Beatrice had not succeeded, the banks would not have lent KKR the funds with which to take over Safeway, Owens-Illinois and Jim Walter. Indeed, just this September 15, KKR announced that the banks had agreed to finance its takeover of Jim Walter Corp. by lending it $2,300,000,000 for that takeover.

The continuing obfuscation here

The respondents are arguing the merits of the case by using footnotes and hope that this Court will initially decide the issues. In reply thereto, the following points should be noted :

1. As early as April 4, 1986, this

petitioner has submitted objections to the Chancellor with respect to BCI's prospectus of March 11, 1986 which was then effective under the Securities Act of 1933. The prospectus covered BCI's Initial Public Offering of the preferred, R. 74a. The Chancellor then had jurisdiction of KKR and was about to consider a "settlement" without any consideration of the facts disclosed in that prospectus. BCI was not named as a party even though it was due to become KKR's vehicle for the takeover. In answer to these objections, the respondents have submitted their April 11, 1986 letter, R. 88a ff. This placed federal questions squarely before the Chancellor whose duty it was to decide them in accordance with Article VI, Section 2.

The Chancellor did not do so. Other courts have done so, Alaska Interstate Co. v. McMillan, 402 F. Supp. 532 (D..Del., 1975), Revlon v. Pantry Pride,

Inc., 621 F. Supp. 804 (D.Del., 1985). If the Chancellor had not wished to express an opinion as to the Federal questions presented, he should have ordered the respondents to remove the case to the United States District Court for the District of Delaware in accordance with 28 U.S.C. Sec. 1441.

Instead, the Chancellor concentrated his attention on, and examined at length, R.12a - 14a, the amended complaint which had not been answered by the defendants and which was the offshoot of collusion between the plaintiffs' and the defendants' counsel. Apparently, the Memorandum of Understanding dated February 1, 1986, had provided for the filing of this sham pleading, the only pleading ever considered by the Chancellor. The Chancellor had to act post haste because at the "fairness" hearing, he was told that the transaction with the banks had

to close within 48 hours. The Chancellor obliged by issuing his memorandum opinion within 48 hours, R. 1a.

The defendants had consented to be sued on certain grounds and none other. It seems that Delaware procedure permits a pleading that has not been answered to serve as the basis for class certification on consent for the purpose of defeating the Federal rights of the members of the class, of shareholders who are not members of the class and of the corporation. Article VI, Section 2 says that this cannot be done. The defendants say it can. This issue should be resolved by the courts below in the first place. See Section 44 of the 1940 Act. KKR is fully aware of the problems it faces with its financing methods. The BCI prospectus of March 11, 1986 states, R.74a :

"In order to effect the Merger, (BCI) expects to obtain approximately $6.4 billion in financing composed of approximately $3.5 billionof indebtedness under a bank credit agreement (excluding a $600 million working capital facility); approximately $2.5 billion from the sale of (BCI's) debt securities; approximately $407 million from the sale of common stock of Holdings; and approximately $10 million from the sale of warrants to purchase common stock of (BCI), all as more fully described below. See "Financing of the Merger".

Question:How could BCI, a $15,000 corporation, obtain bank and debenture credit of $6,400,000,000 for the purpose of "acquiring" Beatrice ? Answer: (a) through the fiction of purpose "loans" in violation of Regulations U and G, by pledging all of the Beatrice stock unlawfully seized from the shareholders (including this shareholder) as collateral for the financing, (b) by

purporting to "delist" Beatrice stock from the N.Y.S.E. and (c) by making a public offering of BCI common stock and warrants without the benefit of registration pursuant to the Securities Act of 1933.

Moreover, in its current tender offer for the Jim Walter Corporation dated August 18, 1987, KKR shows that it is aware of the problems under Regulations G, U and X posed by its financing methods. Please see the statement excerpted from that tender offer, R. 93a. The respondents are blowing hot in this Court. But they are blowing cold in their Jim Walter tender offer materials which are currently aimed at the public at large.

2. This petitioner is not a plaintiff against KKR and Beatrice for which reason the objection procedure was used. Section 327 DCL and F.R.Civ.P. 23.1

both apply to plaintiffs and not to objectors. There is nothing evil about an objector stating his views about a settlement and taking it up on appeal with the appellate courts. If this objector's contentions had been "frivolous" the Delaware Supreme Court would have said so.

A "fairness" hearing is an adversary proceeding where the proponents of a settlement have the burden of showing that the proposed arrangement is "fair, reasonable and adequate". Such a showing cannot be made where, as here, the plaintiffs have an inherent conflict of interest. The plaintiffs here have purported to sue both representatively on behalf of a class (as defined by them, excluding all other shareholders) and derivatively on behalf of Beatrice, the corporation. Under Delaware law, there is a basic question as to whether or not a plaintiff may sue in both capacities,

Harff v. Kerkorian, Del. ch., 324 A. 2d 315. Here, the Chancellor has not resolved the issue, although he identified it, R. 1a - 2a.

Since the plaintiffs and the defendants have lined up on the same side, it is the function of the objector to test the proposed arrangement for compliance with basic principles of equity and with the mandates of Federal law to the contrary. The settlement here purports to extinguish claims arising after April 16, 1986 under State and Federal law. This violates the principle announced by this Court in Transamerica Mortgage Advisors v. Lewis, 444 U.S. 11, 19 (1979):

> We conclude that when Congress declared (in Section 215 of the Investment Advisors Act) that certain contracts are void, it intended that the customary legal incidents of voidness would follow, including the availability of a suit for rescission or for an injunction against the continued

operation of the contract, and for restitution.

The federal securities laws involved here, i.e. the 1940, 1934 and 1933 Acts contain similar provisions. The enforcement of these Federal laws, should not be made "subject" to the ad hoc interpretations of State courts.

3. This Court has granted certiorari in Levinson v. Basic, Inc., 786 F. 2d 741 (C.A. 6, 1986), --- U.S. --- (1986), a case that presents issues strikingly similar to those in the case at bar. Indeed, if the two cases were to be heard together a better understanding of both would be possible and the issues narrowed to those that have to be decided.

If the Basic shareholders are entitled to be heard by this Court, so should the Beatrice shareholders whose claims are about the same. Both classes of shareholders suffer from the same

evil, the unbridled power of the Merger and Acquisition law firms to deprive America's shareholders of their property by permitting their clients, such as KKR, to engage in open violations of law. This pernicious practice, based on scienter, has its genesis in Wolfson v. United States, 405 F. 2d 779 (C.A. 2, 1968), cert.denied, 394 U.S. 946 (1968) and has since been often imitated.

The evils revealed by this record do not stop there. The defendants' law firms work hand-in-glove with the plaintiffs' law firms as their joint Brief in Opposition amply demonstrates. Obviously, the respondents-plaintiffs are no longer independent of the respondents-defendants. Nor were they at any time during the pendency of this litigation.

As the Chancellor has determined, R. 9a, the first of these suits was filed on November 15, 1985. The suit

challenged actions taken by the Beatrice board on November 13 and 14, 1985, R. 8a.

How did a private plaintiff gain access to confidential matters discussed by the board in utmost secrecy ? How did that plaintiff have access to the minutes of that meeting (which had been held in Chicago), arrange for counsel representation, prepare and file a complaint in Wilmington, Delaware within 24 hours of the board meeting ? The minutes of that meeting cover 26 single-spaced typewritten pages, all marked "confidential" and all protected, apparently, by the "confidential" label attached to each.

If this had been a truly adversary proceeding, then the respondents-defendants would have taken the depositions of all the plaintiffs in order to determine how they had breached Beatrice's security. But the record

shows that no such depositions had been taken. Rather, the possibility exists that the board's minutes had been purposely "leaked" to plaintiffs' attorneys so that they could file the first suit on November 15, 1985 and claim standing as "plaintiffs' lead counsel".

All of this has nothing to do with shareholders' Federal rights enacted by Congress over a period of half a century. Rather, on the civil side of the Delaware system of justice, it looks as if Federal securities laws are deemed to be posters on the walls. Drastic steps are necessary if the intent of Congress and the mandates of the Constitution are to be carried out. Only this Court can take such steps.

Conclusion

The Writ of Certiorari should be granted.

Respectfully submitted:

William Leighton

Petitioner

September, 1987

(Letterhead)

POTTER ANDERSON & CORROON

* * * * * * * * * * *

April 11, 1986

HAND DELIVERED

The Honorable William T. Allen
Chancellor, Court of Chancery
Public Building, Wilmington, DE 19801

In re Beatrice Companies, Inc.
Litigation, Consolidated C.A. No. 8248

Dear Chancellor Allen :

On behalf of the Beatrice and KKR defendants, we respectfully submit this letter in response to the issues raised in the letter dated April 4, 1986 from William Leighton, purporting to object to the proposed settlement of the above-consolidated actions. We understand that plaintiffs also intend to address Mr. Leighton's objections. For a number of reasons, the purported objections are both procedurally and substantively deficient, and should be rejected.

First, it does not appear that Mr. Leighton is even a stockholder of Beatrice. His letter suggests that he is not, and a search of the Beatrice stockholder list shows that he was not a record stockholder as of February 20, 1986. If in fact Mr. Leighton is not a stockholder, then he is not a member of the class and lacks standing to complain about the proposed settlement.

Second, the purported objections assume "that BCI (Holdings Corporation) has been properly served with process and is subject to the jurisdiction of the Court." This assumption is erroneous. BCI is not a party to this consolidated action, has never been served with process, and is not before the Court.

More fundamentally, Mr. Leighton's substantive attacks on the legality of this transaction are frivolous. Mr. Leighton states that BCI has violated, or

intends to violate, Sections 7(a), 18 and 49 of the Investment Company Act, assuming, without discussion, that BCI is an investment company for the purpose of the statute. However, BCI is not now, nor will it be after the Merger, an investment company since it meets none of the definitions contained in Section 3 of the Act. At present, BCI has no business activities. After the merger, BCI's business will be the ownership of directly and indirectly wholly-owned subsidiaries which will not be investment companies and which will own and operate the current business of Beatrice Companies, Inc. Beatrice produces and markets food and food-related products, in addition to a broad range of non-food products for use in various consumer, commercial and industrial markets. Since BCI is not an investment company within the meaning of Section 3 of the Act, the

remaining sections referred to in Mr. Leighton's letter have no applicability to the subject transaction.

There is also no basis for Mr. Leighton's claim that BCI is in violation of the margin rules issued by the Federal Reserve Board pursuant to Section 7 of the Securities Exchange Act of 1934, because "it proposes to borrow more than $4,000,000,000 in excess of the amount permitted by Regulation G, or, for that matter, by Regulation U." As the funds to effectuate the transaction are being borrowed only at the time of the merger, such borrowings will not be directly or indirectly secured by any margin stock and therefore will not violate Regulations G or U. On January 10, 1986, the Board issued an interpretation of Regulation G that addressed its applicability to a purchaser of debt

securities to finance corporate takeovers. (12 CFR 207, Section 207.112). This interpretation relates to the application of the margin requirements to two situations involving acquisitions utilizing tender offers. No tender offer is involved in the acquisition of Beatrice by BCI.

For all the reasons stated above, Mr. Leighton's objections are without merit and should be rejected.

(Emphasis supplied).

Respectfully submitted,

POTTER ANDERSON & CORROON

By /s/ Robert K. Payson

Attorneys for Kohlberg Kravis Roberts & Co. and Joel E. Smilow

RICHARDS LAYTON & FINGER

By /s/R.Franklin Balotti/RKP

Attorneys for the Beatrice Defendants

N.B. This document is mentioned at footnote 3 on page 4 of respondents' Joint Brief in Opposition but is not included in the appendix thereto.

Offer to Purchase for Cash

All Outstanding Shares of Common Stock

of

JIM WALTER CORPORATION

at

$60 Per Share Net

by

Hillsborough Acquisition Corporation

a Corporation Formed by

KOHLBERG KRAVIS ROBERTS & Co.

* * * * * * * * *

August 18, 1987 * * *

Federal Reserve Board Regulations.

Federal Reserve Board Regulations G, U and X (the "Margin Credit Regulations") restrict the extension or maintenance of credit for the purpose of buying or carrying margin stock, including (Jim Walter) Shares, if the credit is secured directly or indirectly by margin stock. Such secured credit may not be extended

or maintained in an amount that exceeds the maximum loan value of the collateral.

The definition of "indirectly secured", contained in the Margin Credit Regulations provides that the term does not include any arrangement with a customer if the lender, in good faith, has not relied upon margin stock as collateral in extending or maintaining the particular credit. On January 10, 1986, the Federal Reserve Board announced an interpretative rule relating to the applicability of Regulation G to the issuance of debt securities by a shell corporation to finance the acquisition of margin stock of a target company. The Board stated that it is of the view that such debt securities are generally presumed to be indirectly secured by the maragin stock of the target company for the purposes of Regulation G because the purchasers of the debt securities could not in good faith lend without reliance

on the margin stock as collateral. The Board stated that this presumption would not apply if, among other things, there is a merger agreement between the acquiring and target companies entered into at the time the commitment is made to purchase debt securities or in any event before loan funds are advanced. *** This issue has not, however, been the subject of a judicial determination since the announcement of the interpretative rule.

Prospectus, 23,000,000 Shares, E-II Holdings, Inc. Common Stock ($.01 par value)* * * * * * *

The date of this Prospectus is July 2, 1987. * * ***The Company**

E-II Holdings Inc. (the "Company") is a newly formed holding company that will manage a portfolio of businesses and will seek to enhance its value through leveraged acquisitions, improved management of operations, selective dispositions and corporate restructurings. The Company's experienced management team is headed by Donald P. Kelly, former Chief Executive Officer of Esmark, Inc. and BCI Holdings Corporation ("BCI"). Mr. Kelly will continue to serve as Chairman of the Board of, and hold an equity interests in, BCI.

In April 1986, BCI acquired Beatrice Companies, Inc. ("Beatrice") in a $6.2 billion leveraged acquisition (the

"Merger") led by Mr. Kelly and representatives of Kohlberg, Kravis Roberts & Co., a private, merchant banking firm.* * *

Investment Company Act. The Company does not propose to engage in investment activities in a manner or to the extent which would require it to register as an investment company under the Investment Company Act of 1940 (the "Investment Company Act"). The Investment Company Act places restrictions on the capital structure and business activities of companies registered thereunder and application of its provisions would have a material adverse effect on the Company. Generally an issuer is deemed to be an investment company subject to registration if its holdings of "investment securities" (securities other than (i) securities issued by majority owned non-investment company subsidiaries and (ii) government

securities) exceed 40% of the value of its total assets exclusive of governmental securities and cash items. The Investment Company Act permits a company to avoid becoming subject to such Act for a period of up to one year despite the holding of investment securities in excess of such amount if, among other things, its board of directors has adopted a resolution which states that it is not the company's intention to become an investment company. The Company's board of Directors has adopted such a resolution. If necessary, the Company may invest portions of excess funds in government securities rather than other higher yielding securitiese in order to avoid investment company status. * * * (emphasis supplied).

STATUTES INVOLVED

Investment Company Act of 1940, 15 U.S.C. Sec. 80a-1 et seq.

Jurisdiction of Offenses and Suits. Sec. 44 : The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have jurisdiction of violations of this title or the rules, regulations or orders thereunder, and, concurrently with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by, or to enjoin any violation of, this title or the rules, regulations or orders thereunder. * * *

Judicial Code, 28 U.S.C.

Section 1441. Actions removable generally

* * * (b) Any civil action of which the

district courts have original jurisdiction founded on a claim or right arising under the Constitution, treaties or laws of the United States shall be removable without regard to the citizenship or residence of the parties.

* * *